No. 22,182

United States Court of Appeals

For the Ninth Circuit

SHELDON F. SACKETT, and KVAN, INC., a Washington corporation,
Appellants,

vs.

J. FRANK BEAMAN, and FIDELITY AND DEPOSIT COMPANY OF MARYLAND, a corporation,
Appellees.

REPLY BRIEF FOR APPELLANTS

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Table of Authorities Cited

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REPLY BRIEF FOR APPELLANTS

The most striking aspect of Appellee's Brief is its failure to suggest any reasonable course of action Appellants might have taken concerning their Federal claims other than waiver of their right to present such claims in Federal court.[1] Appellee concedes that when he filed the State action Appellants had no right of removal. He nevertheless suggests that Appellants could have "commenced an action in the Federal Dis-

[1]Appellee's suggestion that the Federal claims might have been raised defensively in State court fails to meet the issues presented on this appeal. Appellants did not wish to litigate their Federal claims in State court. In view of Congress' grant to Federal courts of *exclusive jurisdiction* of actions under the Securities Exchange Act of 1934, it is clear they were not required to do so.

trict Court based on an alleged violation of the federal securities acts . . ." (Brief for Appellee, p. 26). Yet he argues at the same time that the Federal claim is essentially the same claim as that which was litigated in the State action. If Appellee is correct in this position, he is suggesting that Appellants should have engaged in an exercise in futility, for, under Appellee's theory, judgment in the State action, if prior to judgment in the Federal action, would have barred further proceedings in the Federal action on principles of res judicata. Appellee's suggestion thus boils down to a conception that the parties should have engaged in simultaneous litigation in State and Federal courts of corresponding State and Federal claims, with the parties undertaking a race to judgment. Under this theory the first court to reach judgment would prevail over the other.[2] Clearly, a less whimsical approach to the administration of justice under a Federal system exists.

In our view, the procedure adopted by Appellants was both appropriate and reasonable. Immediately

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[2]Appellants could not have protected themselves by filing suit in Federal court and withholding service of process. *Moore Co. of Sikeston, Missouri v. Sid Richardson Carbon & Gasoline Co.* (E.D. Mo. 1964) 237 F.Supp. 817 (although complaint filed within limitation period, action barred by statute of limitation where counsel failed to use due diligence to serve process). Having filed suit in Federal court, they would have been under a duty to prosecute it with diligence. Rule 41(b) Federal Rules of Civil Procedure (defendant may move for dismissal if plaintiff fails to prosecute). Rule 11, Rules of Civil Practice, United States District Court, Northern District of California (each quarter Calendar Judge shall call a convenient number of cases wherein no Memorandum to Set has been filed upon order to show cause why they should not be dismissed for lack of prosecution).

upon discovery of Appellee's fraud, they rescinded the contract under California law by notification to Appellee. When Appellee sued shortly thereafter, Appellants defended and cross-complained on the basis of their rescission and their corresponding right to restitution of the $1,000 down payment. At this point their rescission was effective under California law; no further legal action on their part seemed necessary.[3]

If Appellants were mistaken in believing that on those facts they would obtain relief in the California courts, it was a reasonable and excusable mistake. Appellee has himself cited cases which indicate that at the time the State court action was pending, California law did provide relief in such situations.[4] See Brief for Appellee, page 19. Appellants should not be penalized for a reasonable mistake particularly where, as here, their opponent makes the same error. See *England v. Louisiana State Board,* 375 U.S. 421 (rule enunciated by the court held inapplicable to

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[3]Appellants understandably felt that relief would be forthcoming in the California courts. Appellee had sold closely-held corporate stock to Appellants on the basis of a financial statement *which he prepared* showing the company had a profit of $5,285 when it had actually lost over $37,000.

[4]Appellee even now goes far beyond this contention and argues that under California law the duty of disclosure is as broad as that under Rule 10b-5. This argument is, of course, totally refuted by the opinion dated March 27, 1967, in *Beaman v. Sackett,* 1 Civil No. 23,182, Court of Appeal, State of California, First Appellate District, Division One (unpublished opinion) (C.T. 219):

> "In any event, regardless of plaintiff's status in the corporation, he owed no duty to defendant to disclose information. . . ." (C.T. 234.)

A comparison of this opinion with *Ellis v. Carter* (9th Cir. 1961) 291 F.2d 270 makes this abundantly clear.

Appellants because their conduct was reasonable under the circumstances). In any event, Appellants' conduct does not justify a total forfeiture of their Federal claims.

From December 1961, when Appellants rescinded the contract until May 1965, when the California court entered judgment, the necessity for a Federal action was wholly contingent upon the remote chance that the State suit might be ineffective. Appellants' claim for damages under Federal law, so tenuous and contingent, was too remote and uncertain to support a Federal damage action prior to May 1965, when the State court made its ruling.[5]

Under such circumstances Federal courts are not required to apply the bar of limitations in hidebound fashion. [See *Fishbach & Moore, Inc. v. Int'l Union* (S.D.Cal. 1961), 198 F.Supp. 911, discussed in Brief for Appellants at pp. 13-14]. Rather, they look to the realities or substance of a claimed bar. Thus, in *Burnett v. New York Cent. R.R.,* 380 U.S. 424 (1965), the Supreme Court was presented with the question of the applicability of the three-year F.E.L.A. statute of limitations to a Federal action that was commenced over three years after the cause of action had accrued; the same cause of action, timely filed, in a State court had been previously dismissed by that court. The

[5]Appellee suggests that the existence of Appellants' claim to $1,000 on principles of restitution evidences damage sufficient to start the Federal limitation period. This suggestion ignores the repugnancy between restitution and damage claims. Furthermore, the $1,000 represented only 4% of the purchase price. Viewed in proportion to the entire transaction, it was *de minimis.*

Burnett court conceded that the F.E.L.A. statute of limitations was applicable but held that it was tolled for the period of the pendency of the State court action and until the State court dismissal order became final. The *Burnett* court stated that the basic inquiry is whether Congressional purpose is effectuated by tolling the statute in given circumstances and that examination of the purposes and policies underlying the limitation provision and the substantive act itself were relevant in determining such intent. The court then observed (at pp. 428-430):

> "Statutes of limitations are primarily designed to assure fairness to defendants. Such statutes 'promote justice by preventing surprises through the revival of claims that have been allowed to slumber until evidence has been lost, memories have faded, and witnesses have disappeared. The theory is that even if one has a just claim it is unjust not to put the adversary on notice to defend within the period of limitation and that the right to be free of stale claims in time comes to prevail over the right to prosecute them.' Order of Railroad Telegraphers v. Railway Express Agency, Inc., 321 U.S. 342, 348-349 [64 S.Ct. 582, 586, 88 L.Ed. 788]. Moreover, the courts ought to be relieved of the burden of trying stale claims when a plaintiff has slept on his rights [footnote omitted].
>
> "This policy of repose, designed to protect defendants, is frequently *outweighed,* however, where the interests of justice require vindication of the plaintiff's rights. * * *
>
> "* * * Petitioner here did not sleep on his rights but brought an action within the statutory period

> in a state court of competent jurisdiction. Service of process was made upon the respondent notifying him that petitioner was asserting his cause of action. While venue was improper in the state court, under Ohio law venue objections may be waived by the defendant [footnote omitted], and evidently in past cases defendant railroads, including this respondent, had waived objections to venue so that suits by nonresidents of Ohio could proceed in state courts [footnote omitted]. Petitioner, then, failed to file a FELA action in the federal courts, not because he was disinterested, but *solely because he felt that his state action was sufficient.* Respondent could not have relied upon the policy of repose embodied in the limitation statute, for it was aware that petitioner was actively pursuing his FELA remedy; in fact, respondent appeared specially in the Ohio court to file a motion for dismissal on grounds of improper venue." (Emphasis added.)

If Appellants have slept on their rights in this case, it has been a fitful sleep. The controversy has been intensely and vigorously litigated since its inception by Appellee. In no conceivable sense has Appellee been surprised "through the revival of claims that have been allowed to slumber." On the contrary, Appellee has had every reason to believe that Appellants would pursue all avenues available in their search for justice. It cannot be a surprise that Appellants relied first on State court remedies which they believed to be sufficient and which they were required to present when Appellee sued them in State court. Nor can it be a surprise that when relief was denied

Appellants in State court, they promptly and vigorously prosecuted the Federal remedies which thereupon became actionable.

CONCLUSION

As previously shown, Appellants' Federal claim did not accrue until May 1965 when they first suffered damage as a result of Appellee's conduct. Their action in the court below was therefore timely under any view of the case. Furthermore, even if their claim accrued in 1961, as Appellee contends, the circumstances of this case and the interests of justice require that the statute of limitations be tolled during pendency of the State court litigation.

Clearly Congress never intended that the Federal remedies it established for shady securities transactions be frustrated in the manner here employed by Appellee.

Dated, San Francisco, California,
April 2, 1968.

Respectfully submitted,
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CERTIFICATE OF COUNSEL

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

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